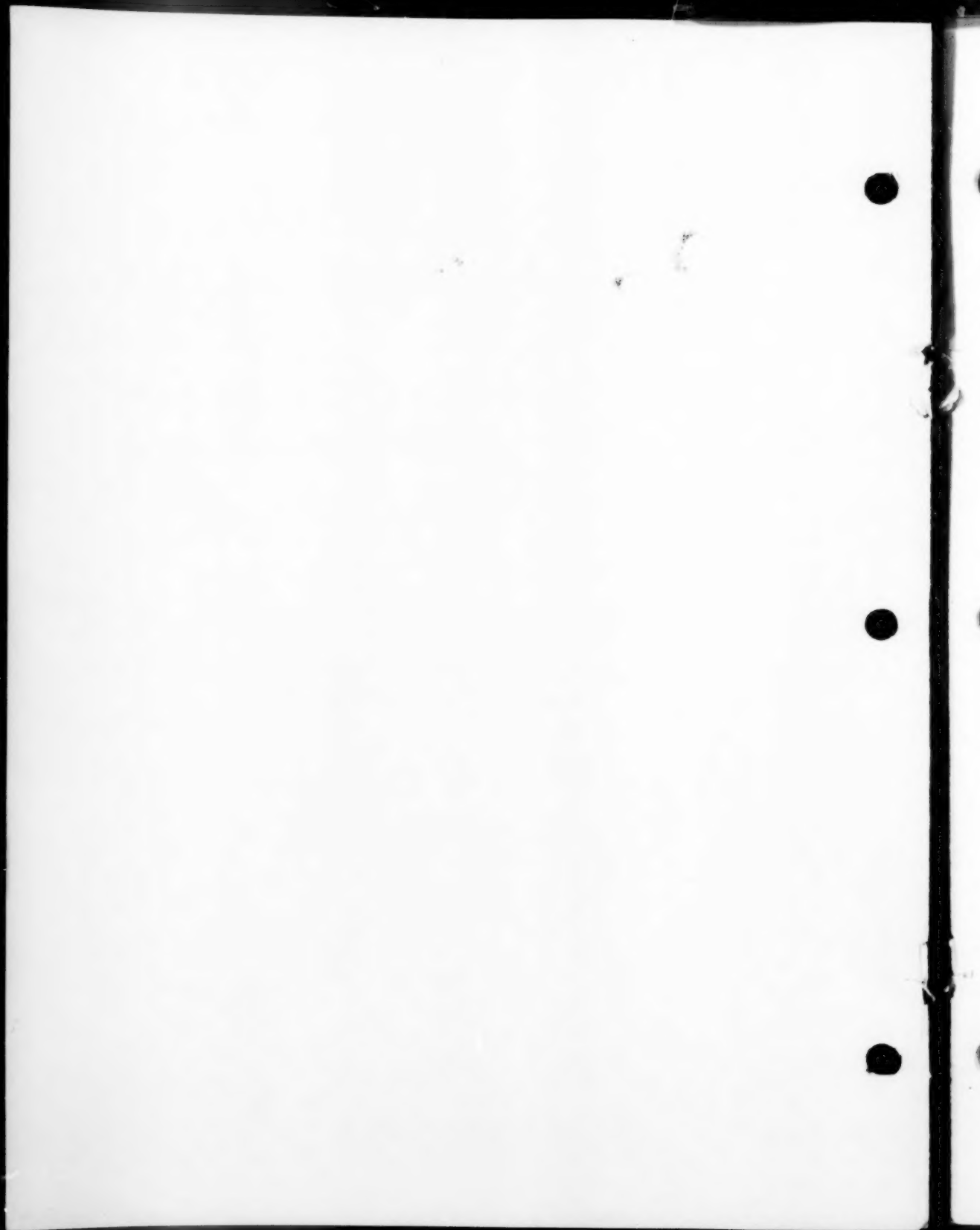


Real Estate
in

1958



REAL ESTATE IN 1958

A Forecast
For Subscribers To

The Real Estate ANALYST

by

ROY WENZLICK

ROY WENZLICK & CO.

REAL ESTATE ECONOMISTS, APPRAISERS & COUNSELORS

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Saint Louis



As I sell

THE OUTLOOK FOR REAL ESTATE IN 1958

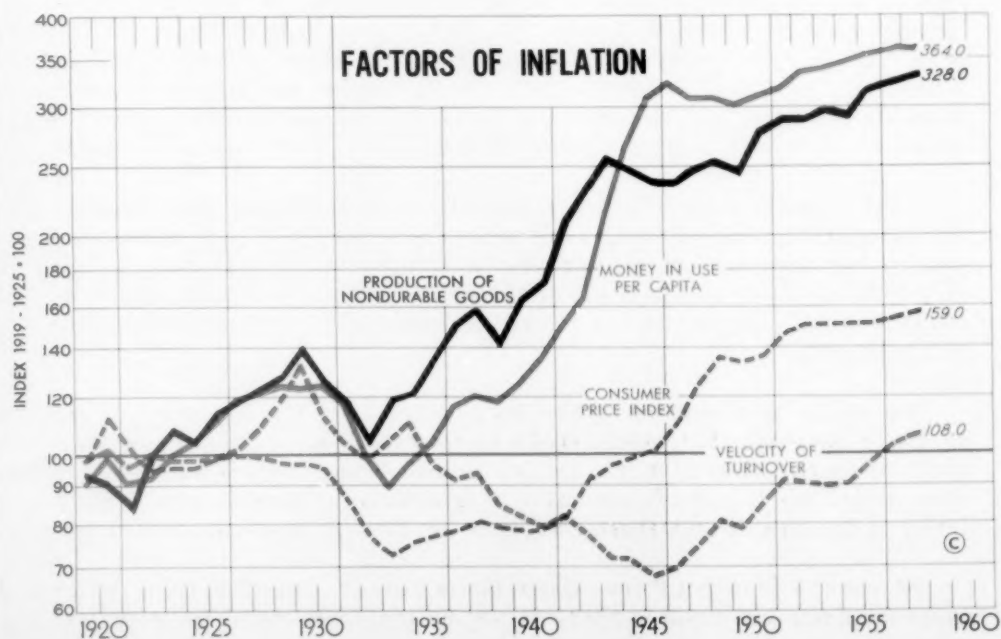
IT now seems that, during 1957, the longest real estate boom in history came to an end. Almost 30 years ago, I found that if voluntary transfers of real estate, in relationship to the number of families, were charted over a long period of years, this chart showed a rhythmic swing above and below a normal line. The last 86 years of this chart are shown on pages 12 and 13 of this report. While the cycles have not been of exactly the same length, height, or shape, to my way of thinking, it requires more credulity to believe that a real estate cycle does not exist than it does to admit that there has been a tendency for the number of sales of real estate to increase steadily year after year in some periods, and to decrease year after year in others.

In economics we are not dealing with an exact science. In mathematics, two and two always make four. Probably in economics the same thing may be true, that a sum total of all causes would result in certain predeterminable results. The difficulty in economics, however, is that the number of causative factors operating on the economy at any time is almost infinite. It may be that through electronic computing, at some time in the future, we may be able to combine in some formula a sufficient number of variables to make of economics a science approaching closer to the exactness of mathematics, physics, and chemistry.

In my opinion, the economist, for the first time in history, sees almost within his grasp the instruments which are necessary to give greater precision to forecasts. Today, there are still great gaps in the information which is needed to give final certainty to estimates of the future, and the quotation still holds that the successful business man is a man who can reach valid conclusions from insufficient data.

There has been a striking similarity in many of these real estate activity cycles of the past. This would hold true for small sections of the cycles. The chart on pages 12 and 13 within the red circles shows a month-by-month decline from a point slightly above normal to a position some months later. The similarity of the areas within these circles is too close to need extended comment.

No one can deny that there may be factors in our present economy which will cause a reversal of trend in 1958. It may be that the Federal Reserve, through



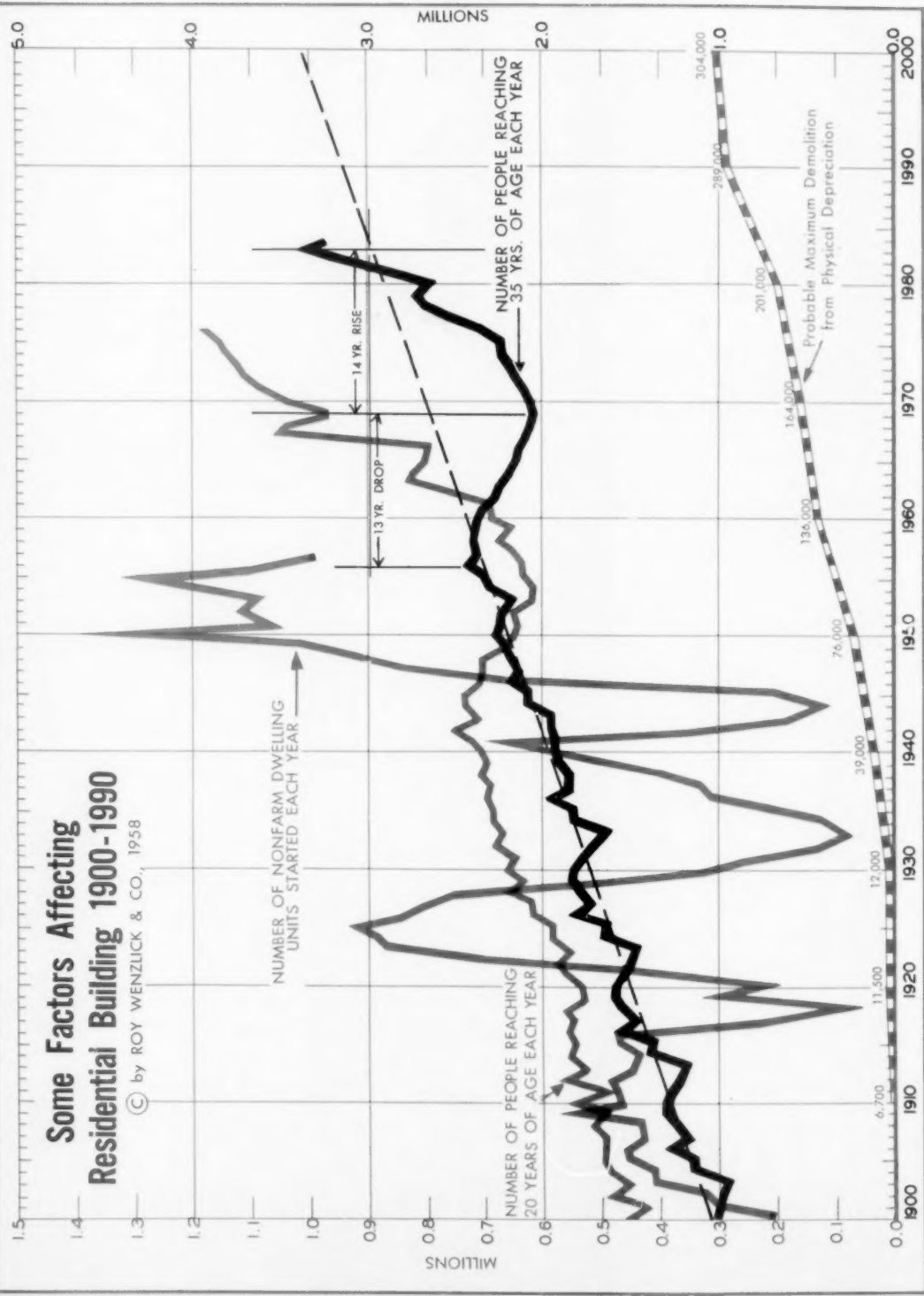
its manipulation of discount rates and of open market operations, can reverse many of the factors which are at present responsible for the beginning of the readjustment phase of our real estate economy. Certainly we know much more about the manipulation of many of the causative factors of inflation and deflation. No one can say with finality, that the trend in real estate sales will follow the patterns of the past, although at present, it seems probable.

As we go into 1958, undoubtedly the subject receiving the most attention is the question of the availability of mortgage money at terms satisfactory to the borrower. Probably at no time are the terms at which money can be borrowed satisfactory to the borrower. Because of the very tight money situation which we have had during 1957, many persons, either correctly or incorrectly, believe that the future of real estate and construction in 1958 depends primarily upon the easing of credit. The chart at the top of the opposite page shows money rates of various types since 1952. Ninety-one-day Treasury bills at the bottom of the chart come closest to being pure interest, and it will be noticed that from the middle of 1954 until the fall of 1957 the trend was almost constantly upward, rising from about six-tenths of 1% in June 1954 to almost 3.7% in October 1957. Then, suddenly, the Federal Reserve reversed its tight money policy, lowered the discount rate, and went into the open market supporting short-term Governments. Almost overnight the Treasury bill rate fell below 3%, and it now seems probable that the policies of the Federal Reserve will be such during the next 6 months or so that currency and credit will be made available to those who can justify its use. Whether this will give the necessary stimulation to the economy is still far too early to tell. It has been said that, while it is possible to accomplish a great deal by pulling on a rope, very little can be accomplished by pushing on it. Some questions of economic behavior are of this type, and it has certainly not yet been proved that re-inflating in an economy heavily in debt will have the same effects secured from the inflationary practices which were consistently maintained for more than 20 years.



Some Factors Affecting Residential Building 1900-1990

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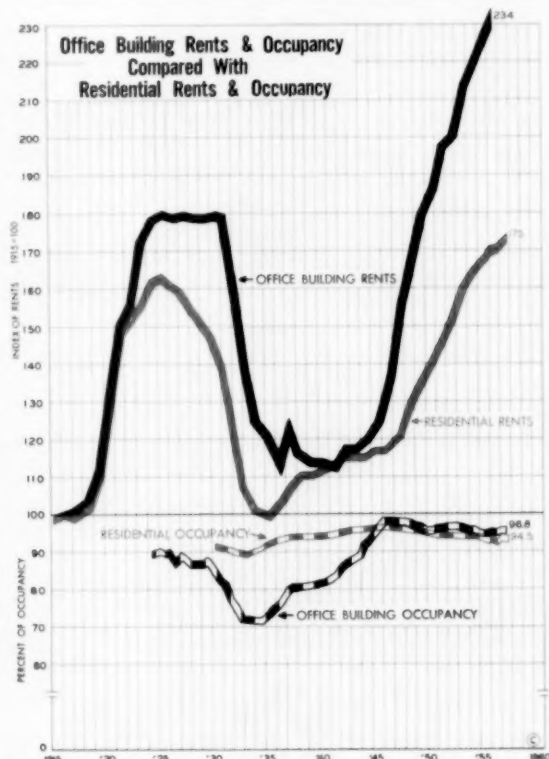
It should be remembered that many countries which have tried to stop economic readjustments by inflating have ended by destroying the value of their money without restoring prosperity.

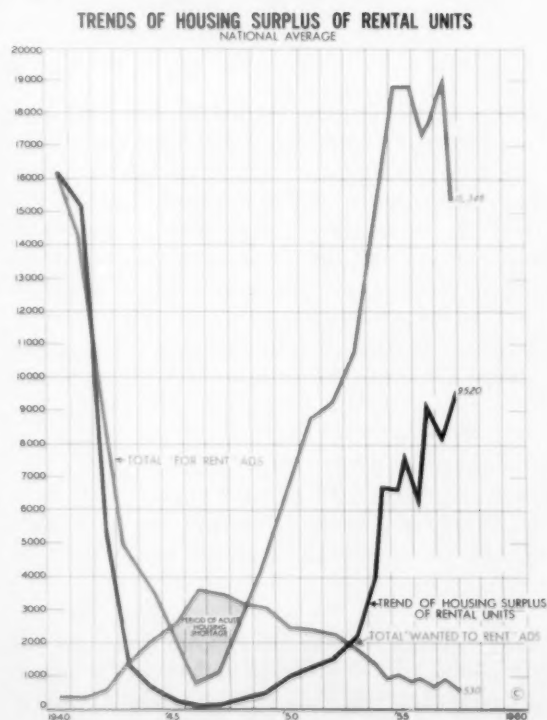
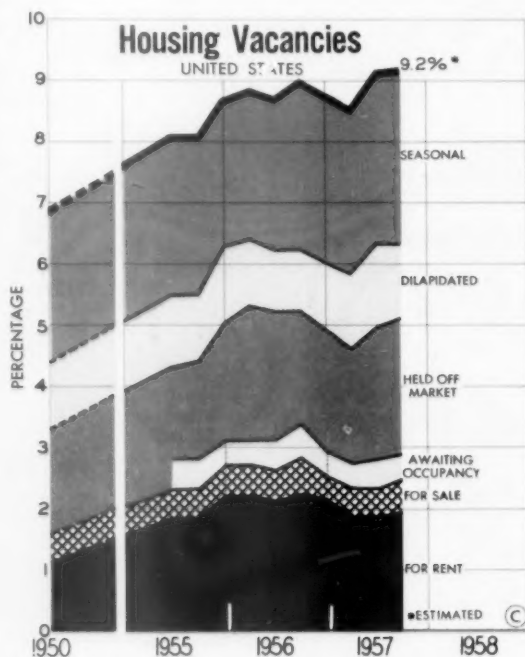
The chart at the top of page 5 shows the effect of the inflation we have had on commodities and services, and on real estate. The market for real estate is undoubtedly severely restricted by the fact that the purchasing power of the dollar for homes, both old and new, has declined by a greater amount than its purchasing power for goods and services.

The chart on the page opposite shows some of the demand factors affecting real estate. Certainly this chart would indicate that, except in the long-term trend, the population figures have not been the determining factor in the volume of residential building. The cyclical fluctuations in the number of dwelling units built show no relationship to either the number of persons reaching 20 years of age each year, or to the number reaching 35 (the average age of home buyers). It shows a much closer relationship to the cycle of real estate activity. I think we must admit that the impending decline in the number of persons reaching 35 years of age each year will affect new building less than the general economic climate and the availability of credit on terms attractive to the public. The rapid increase in the number of 20-year-olds in the 1960's will, together with the increase in the older age brackets, help to increase the demand for rental units above what could be expected for any economic climate which might prevail at that time.

The chart above shows office and residential rents compared with office and residential occupancy for a long period of years. While this chart shows that major fluctuations have occurred and, therefore, probably could again, it also offers considerable encouragement for any period of readjustment which may lie ahead.

When real estate activity went below normal in 1929 (at the beginning of the last major real estate readjustment), residential rents had been falling for a period of 4 years. If our activity chart is indicating that this readjustment has





started, it has done so while rents are still rising. Office building rents had shown no decline in 1929, and as of today they are still rising. Both residential and office building occupancy are at higher percentages than they were then.

Residential vacancy figures were not regularly available in detail until the last few years. The chart opposite shows the breakdown as indicated by the survey of vacancy made by the United States Census. Certainly, there is reason for considerable encouragement in the lowness of their figures.

The lower chart on this page is our attempt to measure the strength of the housing demand for the period since 1940. This chart is based on a count of the classified advertisements in 38 principal metropolitan areas of the United States. The red and green lines show the fluctuations in the ad counts, while the black line is a derived line, attempting to measure the relative amount of the surplus. When it is realized that 1940, the first year on the chart, was one of relative balance between supply and demand, this chart would indicate that the shortage of housing has disappeared, but that we do not have a balance similar to the situation as it prevailed in 1940.

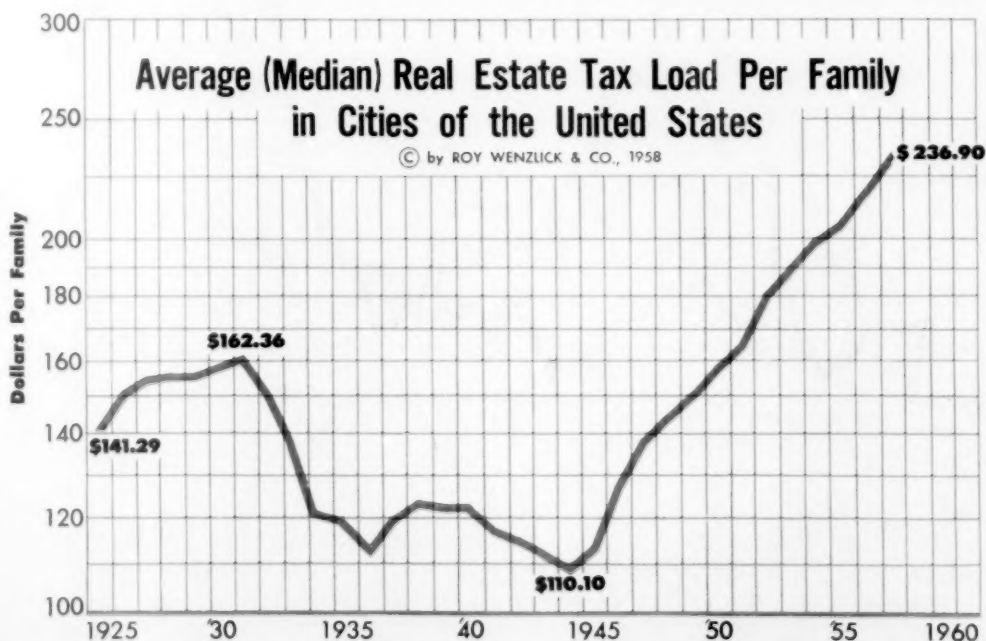
The chart below, while disturbing to the owners of real estate, is always a joy to the real estate forecaster. It is the one forecast that he can make without any danger of being wrong. Real estate taxes will continue to rise! Unfortunately, the cost of government and of schools is still rising. Any effort on the part of the Government to stop a general readjustment would necessarily be inflationary in character, and would result in a resumption of higher prices and costs.

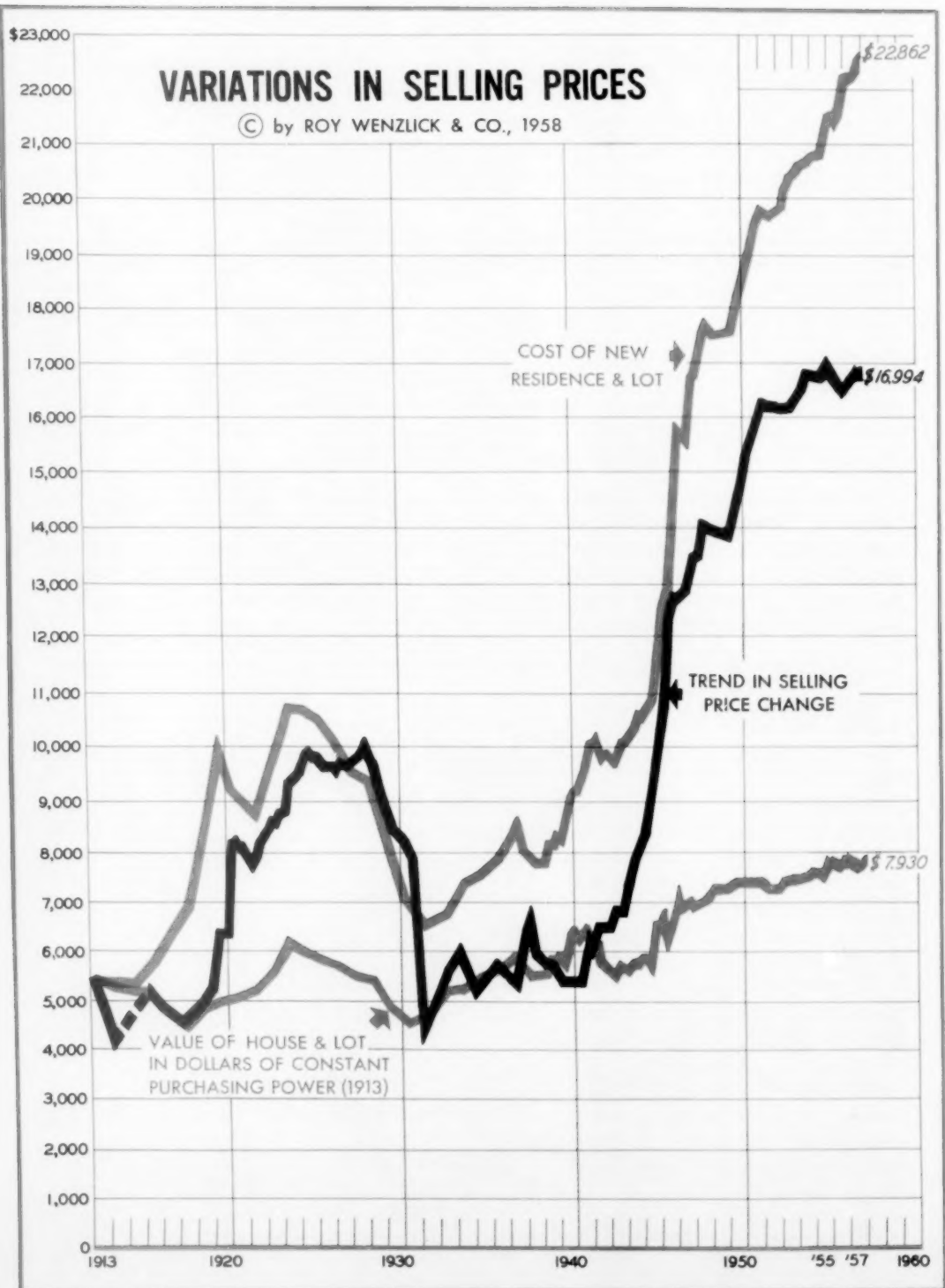
The urban real estate tax load rose, on the average, about \$17 per family during the last 12 months, and there is no reason to believe that the rise will be any less in the year ahead.

The chart on page 10 shows the variation in cost of a new residence and lot in comparison with the selling price of an existing residential building which has been sold at least once before. The surprising thing about this chart is that the selling price of the existing building has continued to hold its own in the period when the number of real estate sales has been dropping and when financing, particularly for older residential buildings, has been difficult.

The behavior of both the building cost figure and the selling price figure is in marked disagreement with that of these figures at the beginning of the last readjustment period. Then, building costs turned down 4 years before real estate activity went below our normal line, and selling prices of older buildings turned down 2 years before. As long as the selling prices of older residences refuse to drop by any great percentage, any readjustment in real estate will be mild.

The green line on this chart shows that the greater part of the change in real

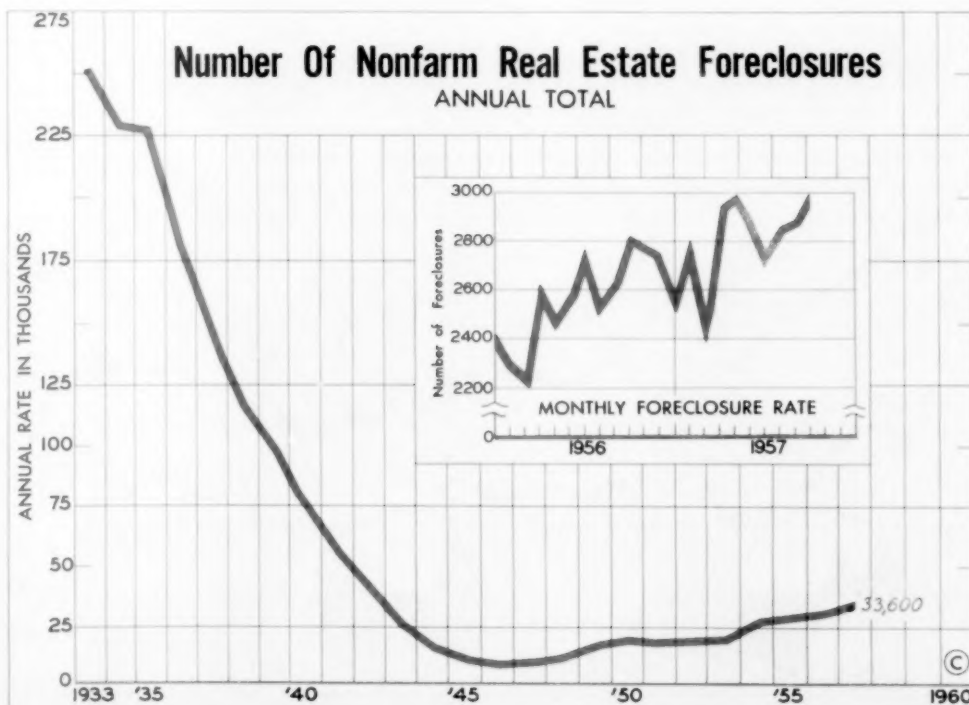


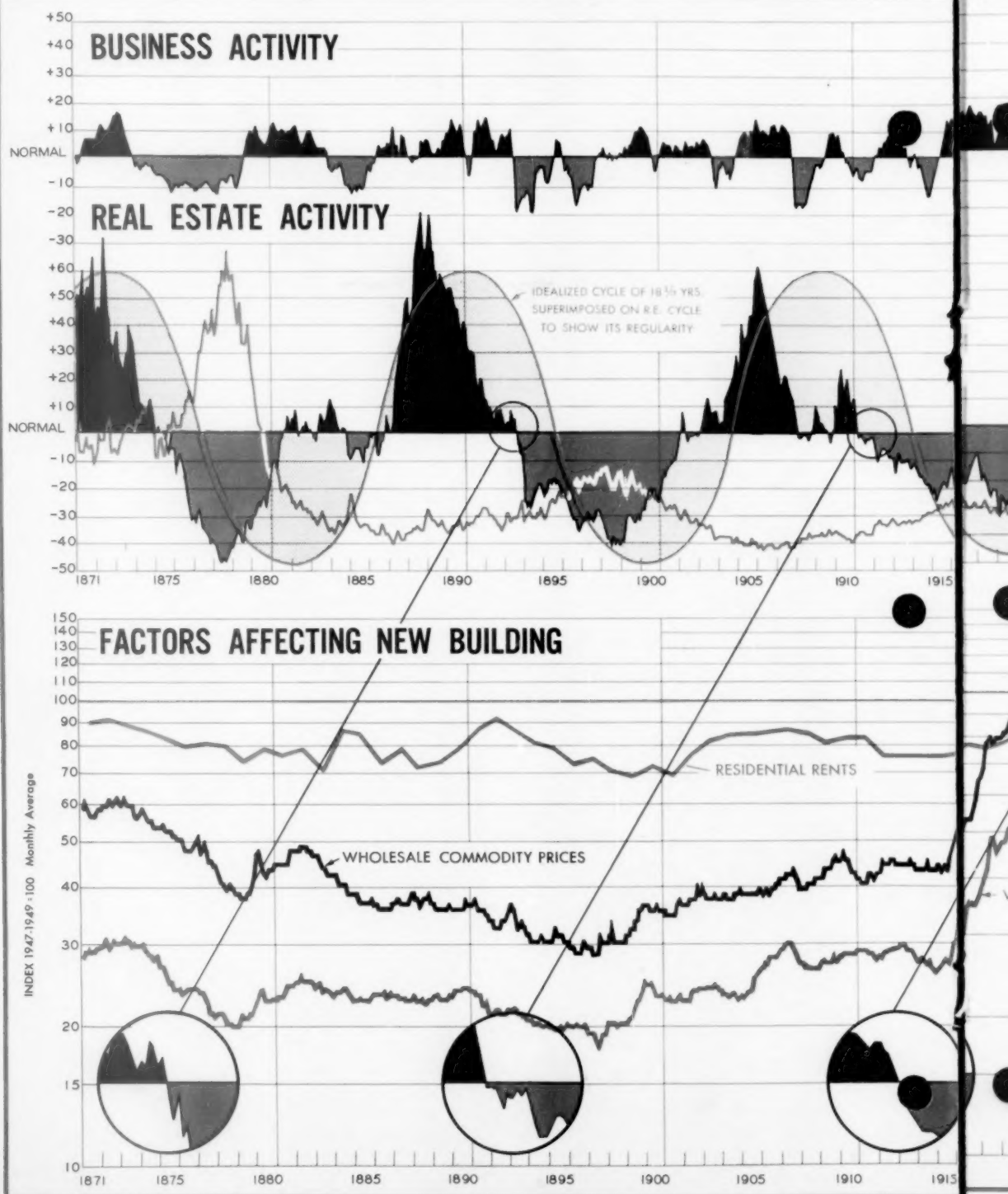


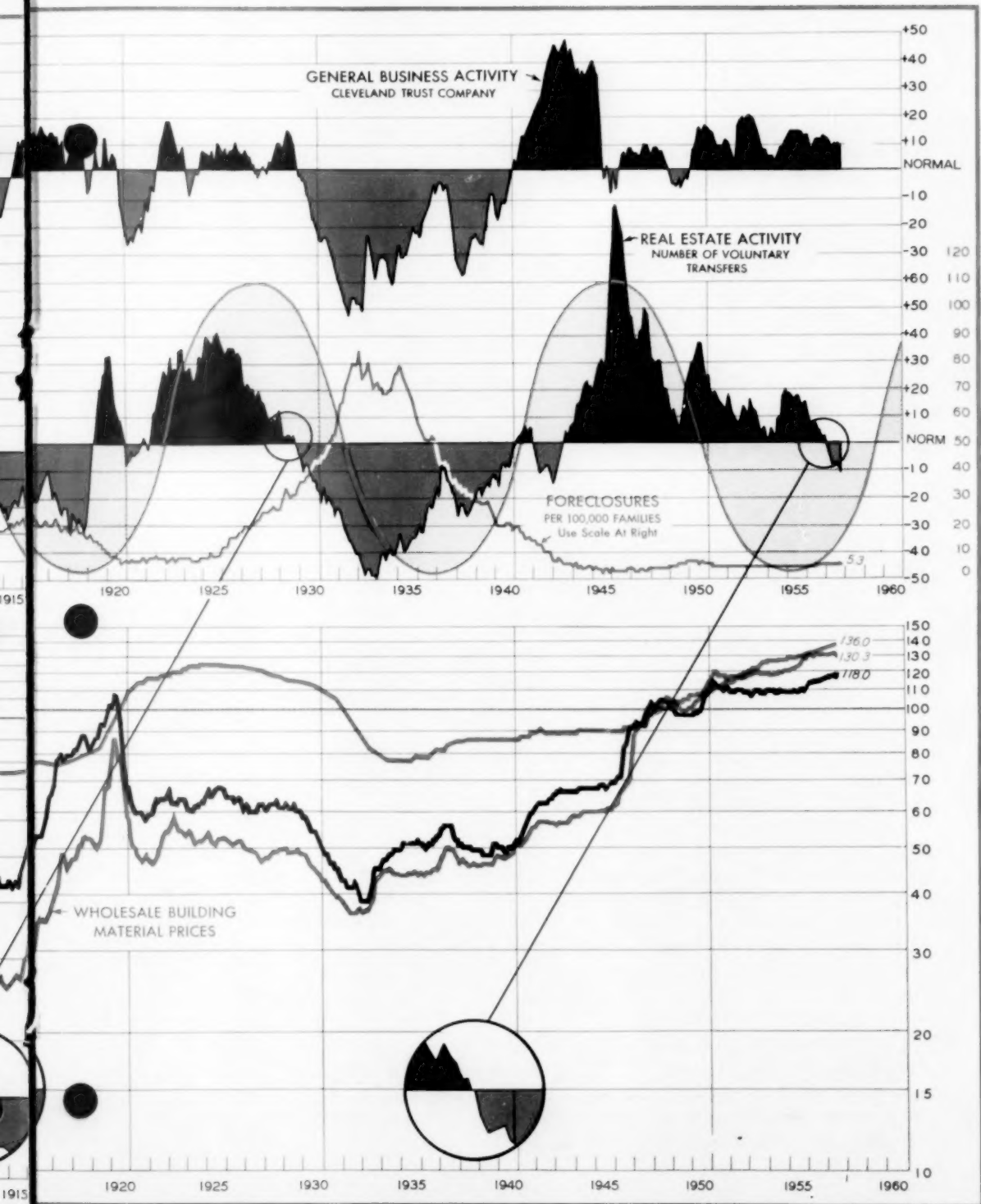
estate values in the last 25 years has been, primarily, a change in the purchasing power of money. This line shows the cost of a new residence and suitable lot had we had a dollar of constant purchasing power over the entire period. On this basis, a house and lot, which in 1913 cost \$5,500, today would cost \$7,930, in place of \$22,862. If we inflate further, as we seem about to do, the cost in dollars will continue up, while the cost in dollars of constant purchasing power will probably go sideways or drift slightly upward.

The chart below shows the number of nonfarm real estate foreclosures by years since 1933, and by months for 1956 and 1957. The monthly figures would indicate clearly that foreclosures are rising, but on an annual basis it will be noticed that they are still remarkably low. By referring to the long chart on pages 12 and 13, it will be noticed that when real estate activity went below normal, at the beginning of the readjustment period of the 1930's, foreclosures were already high, higher than they reached in the World War I depression, and as high as they were in the big depression of the 1890's. In contrast, their present level is surprisingly low.

In spite of the fact that the high foreclosure peaks shown on this long chart in the big depression of the 1870's and the big depression of the 1930's were due primarily to preceding war inflations, I do not expect foreclosures to go very high in any readjustment period ahead of us, although we are again following a







period of war inflation. The monthly payoff loan has almost entirely supplanted the mortgage for a fixed period of years. During these earlier depressions, many mortgages came due in periods in which they could not be refinanced. In any readjustment period, which may be ahead of us, existing monthly payoff mortgages will not have to be refinanced, and so long as the monthly payments can be maintained, will not have to be foreclosed. Since most of these mortgages were made at a time when interest rates were low and financing terms favorable, the owner would probably think that it would be better to continue the payments on a mortgage, even though the value of the property had shrunk, than to relinquish the ownership of the property, with the idea of buying a deflated piece. The less favorable financing terms then available might mean that the monthly payments on the deflated piece would be higher than the monthly payments on the piece which was being relinquished.

I have frequently made the observation that in the period we have come through the ownership of a home by a middle-income family was the best inflation-proof investment that the family could secure. The chart on the page opposite shows what would have happened to the investment of three families during the past 17 years. One family purchased a residence, paying all cash, and still owns that residence today. If the property were sold at today's market value, this family would realize 53.3% more purchasing power than it invested in the property in 1941, in spite of the fact that the building is now 17 years older than it was then. During the entire 17 years there have been only 8 months when the family could not have realized more purchasing power from the sale of the building than it originally invested in it.

The second family invested in "E" bonds in 1941, and has held these bonds up to the present time. The present value of the bonds includes the accrued interest for the 17 years, but even with the interest, the purchasing power which could be derived from their sale is 19.6% below the amount of purchasing power originally invested. The purchaser of these bonds has, then, paid the Federal Government 19.6% to use his money for the past 17 years.

The third family purchased common industrial stocks in 1941, and if these stocks are sold at the market today, this family will receive 65.9% more purchasing power than it put into the market 17 years ago. This does not include the dividends it would have received on these stocks during this period. This is a larger appreciation in purchasing power than the family received that invested in a home, but in more than half the years, the stock purchasers could not have liquidated their stocks for as much purchasing power as they put into them.

In considering the purchaser of a home, we have not given any credit for the rental value of the building during the 17 years, nor have we mentioned that the home owner could have deducted his real estate taxes as an expense in making his income tax return. On the other hand, he could take no deduction for rent payments if he did not own his own home.

If the period ahead is to be an extended deflationary period, the pattern which developed during the past 17 years would not be repeated, but from the recent action of the Federal Reserve Board, it looks very much as if the sound money policy has been put back on the shelf, with the prospect, for at least the short run, of more inflation.

The big question at the beginning of each new year is how much building volume can be done. The chart and table on pages 18 and 19 show the volume of building from 1945 through 1957, with 1958 estimated by the Department of Labor and the Department of Commerce. I think it is probable that, while 1958 will exceed 1957 in dollar volume, the excess will not be as great as 5%, the amount shown in this estimate. I also doubt whether the dollar volume of new private residential construction will exceed 1957 by 6%, and I doubt whether office building and warehouse construction will exceed 1957 by as much as 8%. While undoubtedly public residential building will be very much greater than it was in 1957, I will be surprised if, at the end of the year, it has beaten 1957 by 68%.

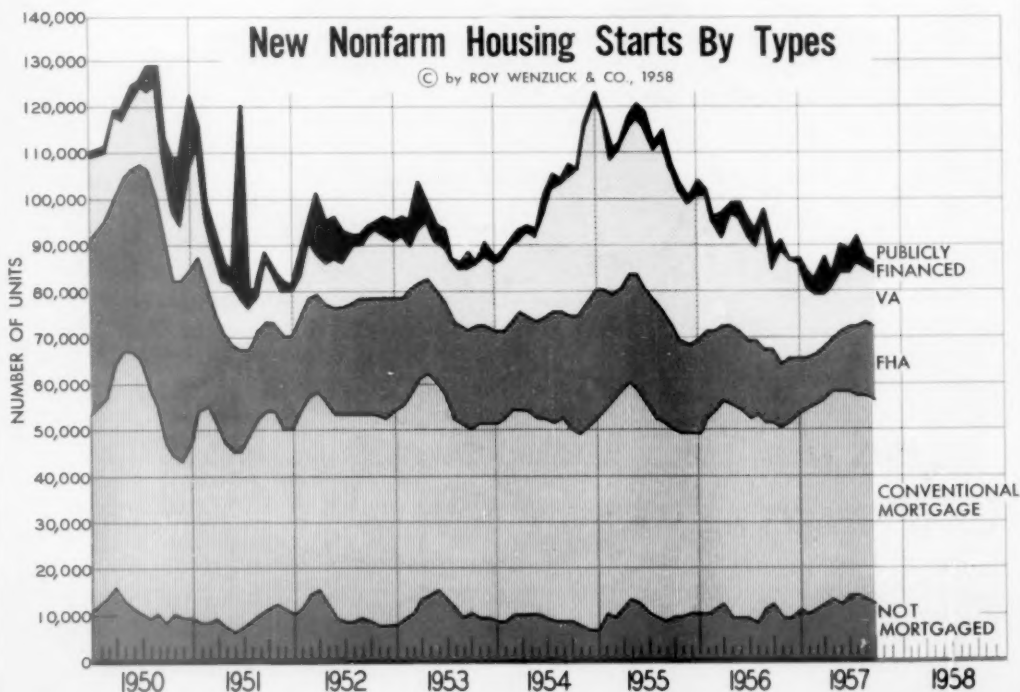
The chart at the bottom of the following page shows the number of new non-farm housing starts since 1950, classified by type of financing. This chart would indicate that at the present time, on the average, we are building about 13,000 new dwelling units a month which do not carry any mortgage. This amount of nonmortgaged home building has fluctuated slightly from month to month, but has generally varied somewhere between 6,000 and 16,000 units per month. The



biggest surprise revealed by this chart is the fact that the volume of home building financed without Government help of any sort, by conventional mortgage or with no mortgage, has shown relatively little fluctuation from 1950 to the present. This type of private home building has generally accounted for from 50,000 to 60,000 dwellings per month, or from 600,000 to 700,000 units per year, year in and year out. FHA and VA combined have accounted for less than half as many during the past year. The chart shows clearly that the fluctuating part of the home building market during the past 7 years has been the part financed with the low downpayment terms offered by the FHA and VA. If the FHA interest rate could be freed to move up or down with the market, either by freeing the rate from artificial control or by removing discount limitation, it could be a larger factor in maintaining the volume of private residential building.

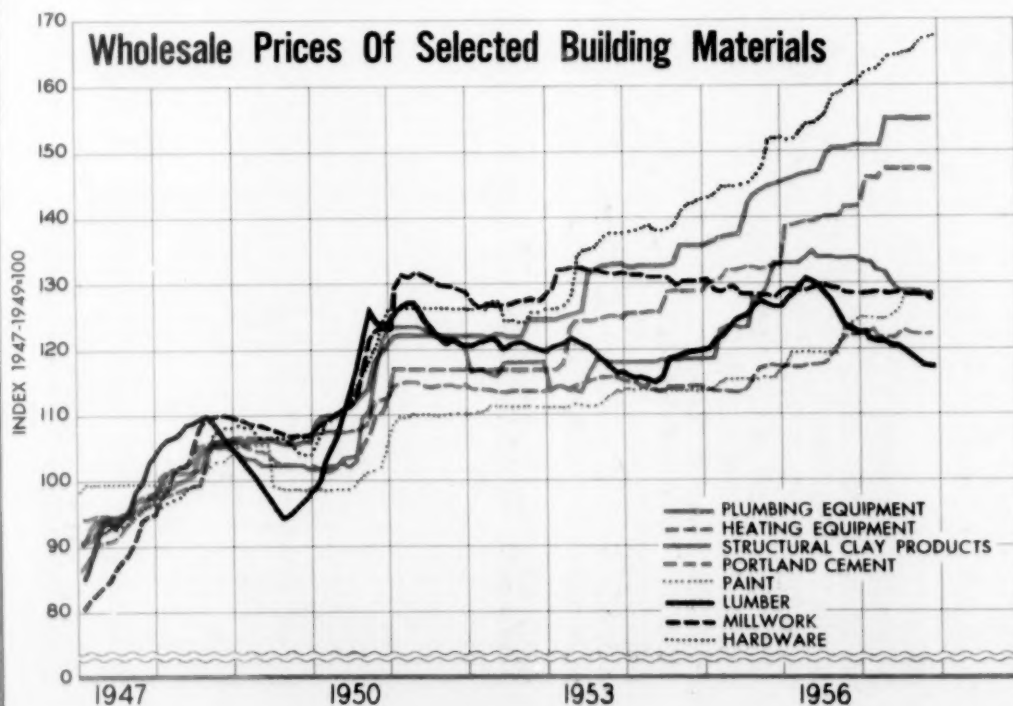
As conditions exist today, it seems that the largest volume of private residential building possible would be an amount almost equal to 1957, or about 980,000 units, with the possibility that private units could conceivably fall as low as 900,000, the current forecast of the home builders.

The total cost of building will probably inch up very little in 1958, with many of the materials showing weakness, but offset by some slightly higher wage scales. Labor efficiency will increase, however, as it always does in periods of increasing unemployment.



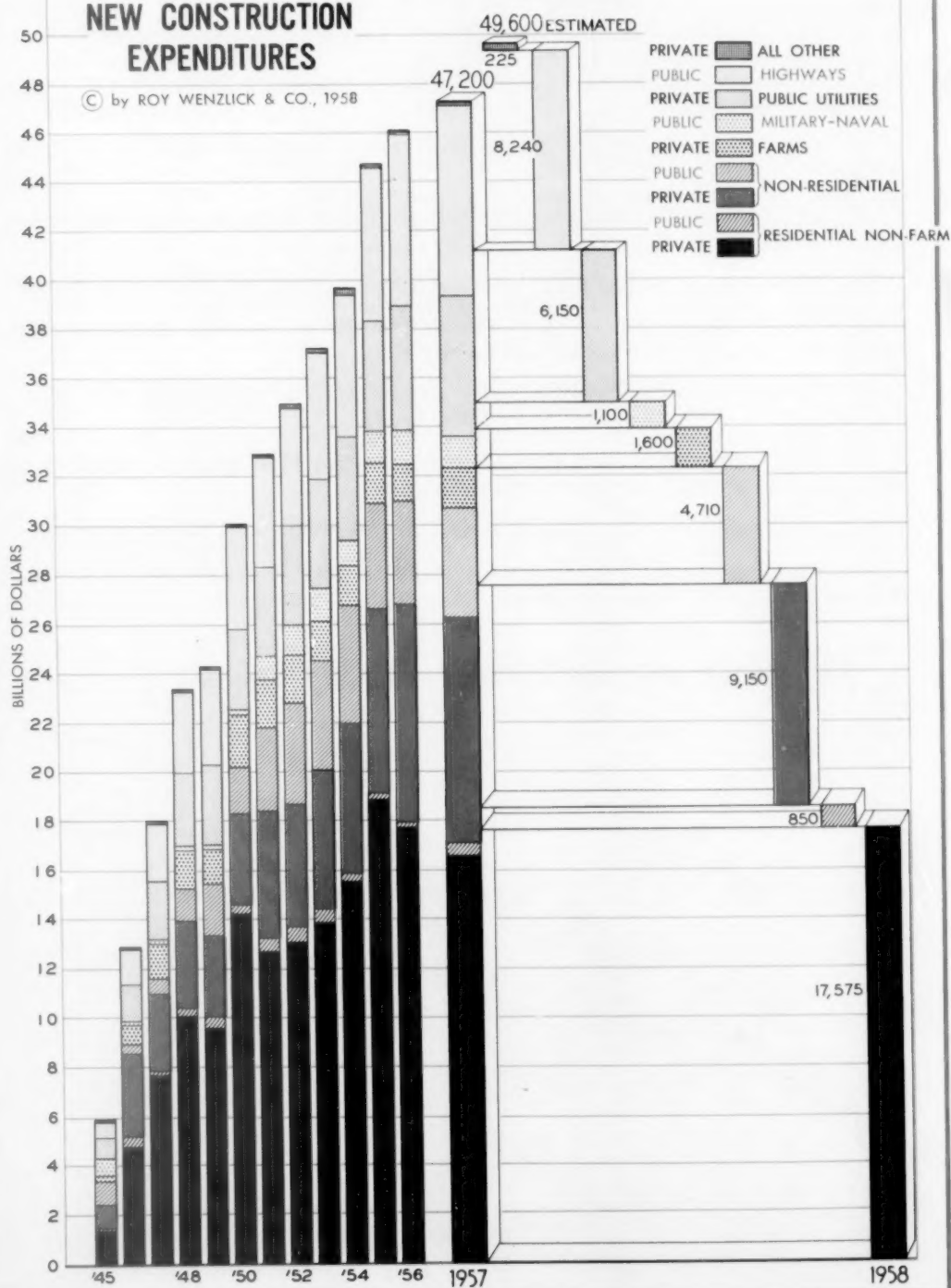
SUMMARY OF URBAN FORECASTS

1. The number of real estate sales will decrease in 1958.
2. Residential vacancies will increase gradually during the year; rents will increase very slightly.
3. The selling prices of used single-family houses will decline by a small amount.
4. Building costs of residences will show little change; other building costs a slight increase.
5. Office building vacancy will increase slightly; rents will show little change.
6. Retail stores, not in the downtown district and not in logical shopping subcenters, will develop considerable vacancy.
7. The prices of vacant lots suitable for residential building will show some softening.
8. The number of private dwelling units built in 1958 will be fewer than in 1957; modernization and repair will be higher.
9. The percentage of dwelling units built for rent will increase in 1958.
10. Mortgage money will be easier but not easy. Mortgage interest rates will remain at about their present level during the year.



NEW CONSTRUCTION EXPENDITURES

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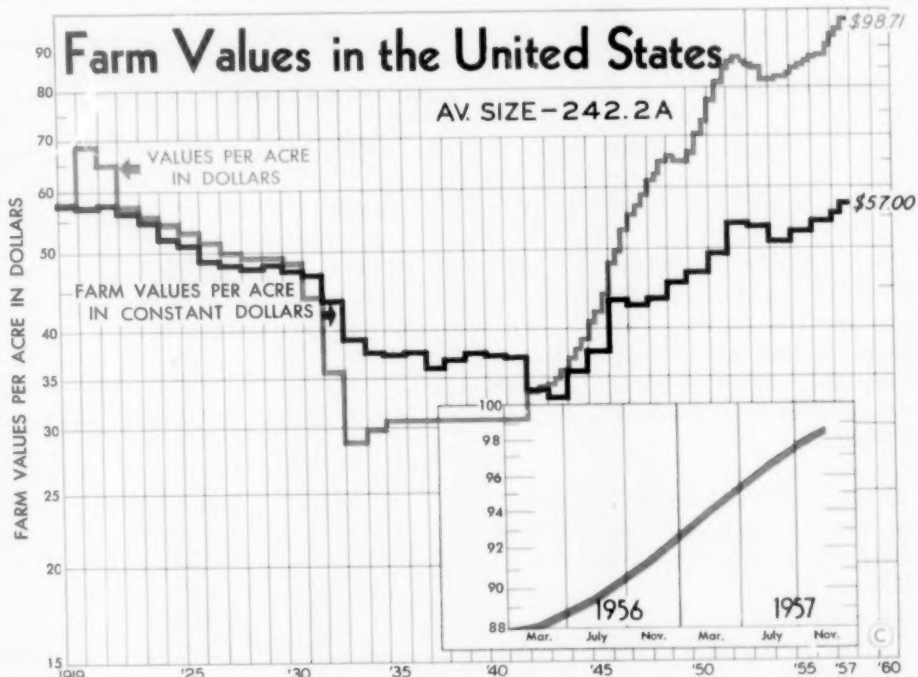


NEW CONSTRUCTION IN CONTINENTAL UNITED STATES

1957 and Outlook for 1958 (Millions of dollars)

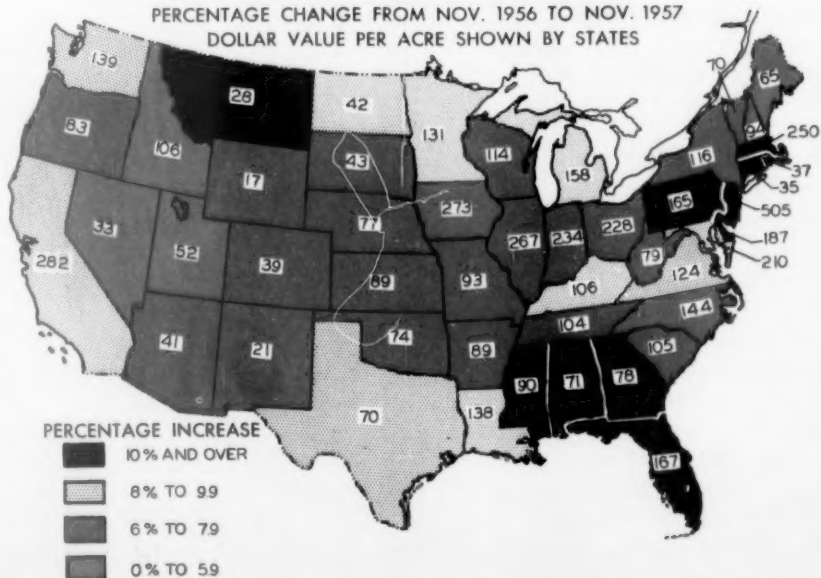
Joint estimates of the Department of Labor and the Department of Commerce

Type of construction	1957	1958	% change
TOTAL NEW CONSTRUCTION	47,200	49,600	+5
PRIVATE CONSTRUCTION	33,300	34,700	+4
Residential buildings (nonfarm)	16,530	17,575	+6
New dwelling units	12,125	12,800	+6
Additions and alterations	3,915	4,250	+9
Nonhousekeeping	490	525	+7
Nonresidential buildings (nonfarm)	9,155	9,150	less than $\frac{1}{2}$
Industrial	3,170	2,875	-9
Commercial	3,585	3,775	+5
Office buildings and warehouses	1,870	2,025	+8
Stores, restaurants, and garages	1,715	1,750	+2
Other nonresidential buildings	2,400	2,500	+4
Religious	870	870	0
Educational	525	540	+3
Hospital and institutional	505	590	+17
Social and recreational	300	300	0
Miscellaneous	200	200	0
Farm construction	1,600	1,600	0
Public utilities	5,825	6,150	+6
Railroad	450	400	-11
Telephone and telegraph	1,075	1,000	-7
Electric light and power	2,100	2,350	+12
Gas	1,800	2,000	+11
Other public utilities	400	400	0
All other private	190	225	+18
PUBLIC CONSTRUCTION	13,900	14,900	+7
Residential buildings	505	850	+68
Nonresidential buildings	4,470	4,710	+5
Industrial	455	450	-1
Educational	2,830	3,000	+6
Hospital and institutional	330	340	+3
Administrative and service	430	470	+9
Other nonresidential buildings	425	450	+6
Military facilities	1,275	1,100	-14
Highways	4,825	5,500	+14
Sewer and water systems	1,345	1,270	-6
Public service enterprises	395	400	+1
Conservation and development	965	950	-2
All other public	120	120	0



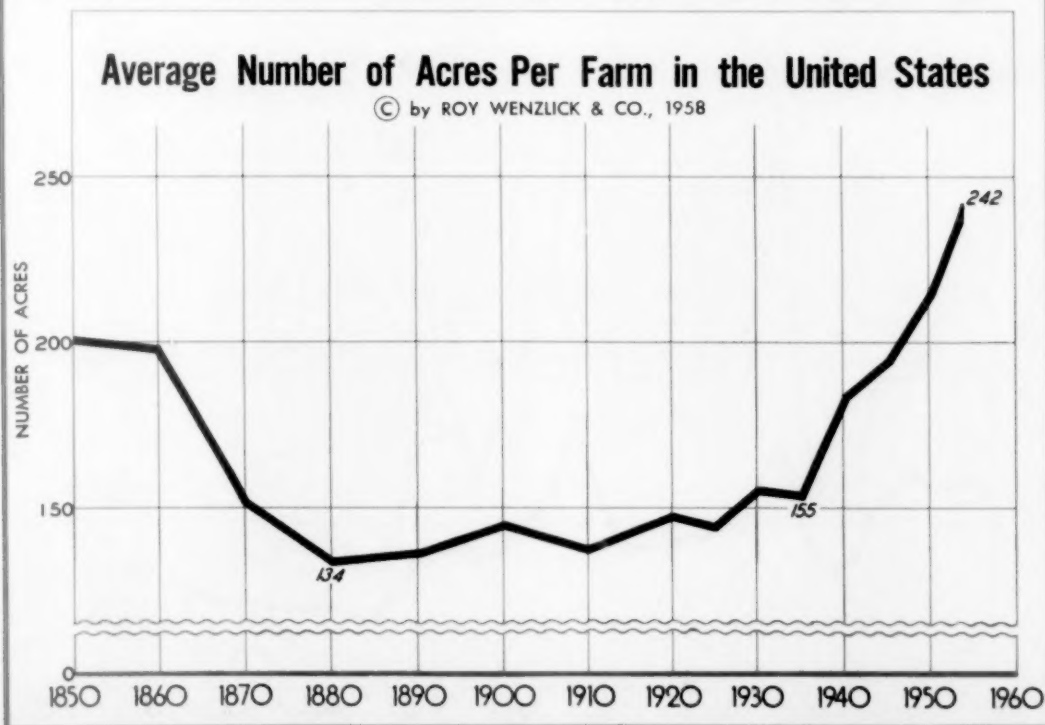
Percentage Change in Dollar Value of Farm Land By States

PERCENTAGE CHANGE FROM NOV. 1956 TO NOV. 1957
DOLLAR VALUE PER ACRE SHOWN BY STATES



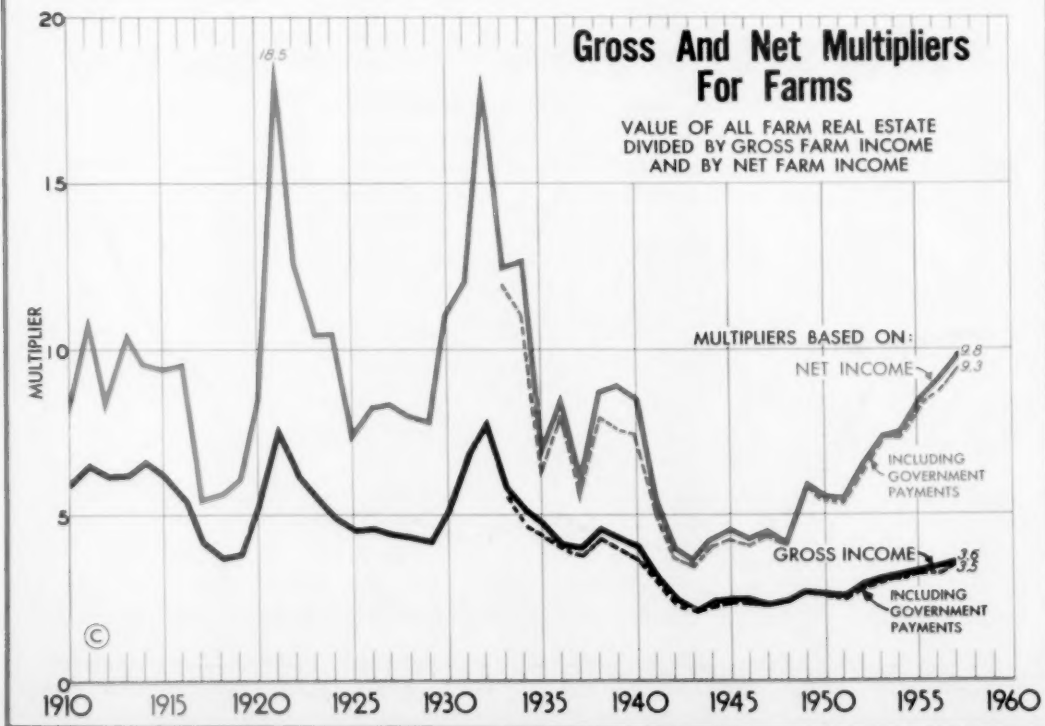
Farm values in the United States have continued upward, rising approximately 8% during the past year. The red line on the chart at the top of the page opposite shows farm values in the United States expressed as values per acre in dollars. In spite of all of the difficulties under which the farmer has operated, farm land is still sufficiently attractive that it is constantly being bid higher. The black line on this chart shows what the fluctuation in farm values per acre would have been had we had a dollar of constant purchasing power in the United States since 1919. On this basis, a large part of the change in farm values is shown for what it actually is - a change in the purchasing power of money. Farms have sold for more dollars because dollars bought less of almost anything available for purchase. If the purchasing power of the dollar had remained constant since 1919, farms would sell today for slightly less than they sold for then. At no time during World War II or during the Korean War did farm values go as high in constant dollars as they were right after the end of World War I.

In using this farm value chart it should be kept in mind that these per-acre prices on farms include the value of the improvements. The chart at the bottom of this page shows how the size of farms has varied over a period of more than 100 years. In 1850, the average farm in the United States contained slightly more than 200 acres. By 1880, because of the reconstruction in the South which followed the Civil War and the cutting up of many large plantations into smaller farms, the average size of farms had dropped to approximately 135 acres. From



that time on, however, there has been an upward drift in the average size of farms in the United States. This has been particularly noticeable since 1935. In 1935, the average farm in the United States contained 155 acres. By 1940, 5 years later, the average size had risen to 174 acres. By 1945 it had risen to 195 acres, by 1950 to 215 acres, and by 1954, the last year for which figures are available, to 242 acres. This would indicate that during the past 20 years a strong part of the demand for farm land has come from the owners of adjoining property. With modern machinery, small fields cannot be worked as economically as large ones, and in order to reduce the cost of production it has been necessary for successful farmers to increase the size of their operations. This increase in size has not yet stopped, and I think that the owner and operator of a small farm is going to find competitive conditions against him in the years ahead. The trend which has been continuing during the past 40 years will continue for at least the next 10 or 20. We are seeing on the farm the same transition which has already made it difficult for the small independent retailer to continue in competition with larger, more efficient units.

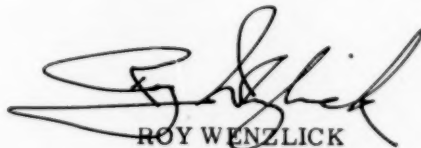
The appraiser of urban real estate has had various rules of thumb which have acted as a rough guide to value. The chart below is an attempt to find out what relationship there has been in the United States over a period of years between the gross marketings and the net income from farms in comparison with the dollar prices at which farms were selling. The black line on this chart shows the number of times by which the gross income would have to be multiplied



to equal the average value of a farm. It will be noticed that, if at the present time the gross annual income is multiplied by about $3\frac{1}{2}$, it will equal the value of the farm. The highest this multiplier has ever gone was in 1921 and 1932, when the multiplier stood at 7.6 and 7.8. It has not been above 3.6, however, since 1941. If the same study is based on net income for all farms in the United States, at the present time these farms are selling for 9.8 times their net income. In 1921 this figure went to $18\frac{1}{2}$ times, but has not been above its present level since 1935.

Since this chart covers all types of farms in all parts of the United States, it does not seem to be a very usable tool for estimating value. We are, however, at the present time preparing multipliers for all of the various types of farm lands, and it seems to me that these may be of some real worth.

The price at which farm lands will sell in the future in most cases will depend on whether we inflate or deflate our money supply. If the recent action of the Federal Reserve indicates that monetary manipulations are to be used to stop the readjustment, at least temporarily, there may be some chance that farm land values will show considerable increase in the years ahead. If, however, we try to control inflation, it is probable that little further advance can be expected in the near future.



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